Pavilion REIT's tenancies on the rise

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KUALA LUMPUR: Kenanga Research is keeping Pavilion Real Estate Investment Trust (REIT) as its top sector pick on the back of its earnings resilience.

"We believe Pavilion REIT's premium retail assets are less vulnerable to downward pressure on occupancy and rental rates amidst rising headwinds in the retail sector on the back of sustained high inflation that hurts consumer spending," it said in a note.

The research firm, which has an "outperform" call on Pavilion REIT, said the REIT's FY23 results met expectations with a notable pick-up in occupancy rates, along with a return in overall consumer spending appetite.

The REIT's FY23 core net profit of RM285.3mil made up 100% of Kenanga's full-year forecast and 101% of consensus' full-year estimate.

Kenanga said the final distribution per unit of 4.6 sen brought FY23 payout to 9.01 sen, which was within the research firm's expectations.

On outlook, the research firm said Pavilion REIT's assets appear to be seeing higher tenancy ratios and encouraging footfall.

In December 2023, Pavilion KL recorded 95% occupancy, up from 92% in 2022, The Intermark saw an increase to 90% tenancy from 87% and Da Men Mall saw 73% tenancy compared to 65%.

"That said, we hold our breath for a meaningful increase in rental rates as it could be fluid in accordance to market conditions, which we anticipate could face resistance in the near term, no thanks to the implementation of new taxes and targeted subsidies," said Kenanga.

It added that it is also encouraged by Pavilion REIT's rights of first refusal granted for the possible acquisition of fahrenheit88 mall, located directly opposite its key Pavilion KL asset.

Kenanga tweaked its FY24 earnings projection by minus-1% as it incorporated Pavilion REIT's FY23 full-year numbers.

Meanwhile, it introduced its FY25F earnings, which forecast a modest earnings increase of 4% as tenancy levels and rental rates may remain stable in the medium term.

"We raise our target price to RM1.51 (from RM1.47) as we roll over our valuation base year to FY25F with a DPU of 9.1 sen.

"This is against an unchanged target yield of 6% (derived from a 2% yield spread above our 10-year MGS assumption of 4.0%)," it said.

Kenanga said the low yield spread is to reflect its prime asset portfolio as anchored by Pavilion KL and Pavilion Bukit Jalil.

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